

## Autumn 2012

### Remuneration of shareholder employees

The *Penny and Hooper* decision is a landmark tax avoidance case that has implications for small businesses operating through a company or trust. Essentially, the Supreme Court decided in favour of Inland Revenue, concluding that setting artificially low salaries amounted to tax avoidance.

Penny and Hooper were two orthopaedic surgeons, each earning taxable income of between \$600k and \$850k a year. They restructured their businesses into companies with a family trust owning most of the shares. They provided their services to the companies in return for salaries of \$100k - \$120k each year. The balance of the company's income was declared as dividends to the family trust which the surgeons drew from regularly.

Each year tax of between \$20k and \$30k was saved by having the profits after salaries taxed at the trustee rate rather than at the surgeons' individual top personal tax rates. The court found these savings a 'more than merely incidental' reason for their low salaries.

The IRD has put businesses on alert and is actively reviewing those operating through a company or trust where the income is generated from services provided by an individual, and the individual's salary is unreasonably low. Although there may be

## Risk and Reward



good reasons for setting the salary low in a particular year, e.g. adverse business conditions, or a planned expansion of the business, in some cases the sole reason for the salary level is to take advantage of the lower tax rate that applies to companies.

The IRD is entitled to go back four years into a business' records, but have publicly confirmed that where a 'voluntary disclosure' is made, only the last two income tax returns will be reassessed. A voluntary disclosure might significantly reduce IRD penalties or avoid them entirely.

Whenever we're discussing your business we'll look at this for you. In the meantime, if you are concerned and would like to discuss this with us, please do contact us.

## Year End Processes

With the end of the financial year rapidly approaching it is worthwhile to review our processes for dealing with your 2012 financials.

Over the next few weeks we will send everybody a letter **advising which month your financials are scheduled** to be prepared. This scheduling ensures we have staff available to prepare your financials when you send your information in and **will speed up our turnaround time**. Ingrid will be joining our firm at the end of March and managing this process for us. Once you have received your letter advising the month we require your information, If you would like to change the scheduled time please contact Ingrid and she will do her best to arrange a time that best suits your needs.

As we find the checklists tend to get mislaid later in the year, we will not send out our **full checklist** at this stage and will send it out **closer to your preparation month**. We are hoping that this will increase the return rate of the checklists as well as the level of details supplied.

There is some information you need to gather at **31 March** to have available when completing the checklist and on page 3 of this newsletter we have included a reminder about this.

This year we will supply **customised checklists with details of the critical information** that we require. To keep fees down we need to ensure we have all information on hand before starting your financials.

If you have any questions, or if you wish to change the month of preparation, please do not hesitate to get in touch.

## Working For Families

From April 1 2012 many of the small changes to Working For Families signalled last year come into effect:

- The family tax credit amount for children under 16 will rise for inflation:

Qualifying Child	Current amount	New amount
First child under 16	\$4,578	<b>\$4,822</b>
Second child if under 13	\$3,182	<b>\$3,351</b>
Second child if 13 - 15	\$3,629	<b>\$3,822</b>

- The net income level guaranteed by the minimum family tax credit will rise from \$22,204 to \$22,568
- The abatement rate will increase from 20 to 21.25 cents in the dollar
- The abatement threshold will decrease from \$36,827 to \$36,350

## KiwiSaver

As of 1 April 2012 employer contributions will no longer be tax free. Employer Superannuation Contribution Tax will apply at the employee's marginal tax rate.

## Minimum wage

As of 1 April 2012 the minimum wage will increase from \$13.00 per hour to \$13.50 per hour.

Training and new entrants' minimum wages will increase from \$10.40 to \$10.80 - 80 percent of the adult minimum wage.

## New GST rules for multi-use assets

New rules came into effect 1 April last year replacing the old change-in-use rules by apportioning input tax deductions in line with the actual use of the goods and services. As the 2012 financial year closes, the new rules will be applied for goods and services acquired on or after 1 April 2011. In subsequent periods, when a change to the actual taxable use occurs, from what was first intended, a GST adjustment within an adjustment period must be made (a number of exemptions may apply).

There are a maximum number of adjustment periods according to the asset's value or estimated useful life and special 'wash-up' rules apply when goods and services that have been subject to the apportionment rules are sold or the person deregisters.



**Death and taxes may be inevitable, but they shouldn't be related. J.C. Watts, Jr.**



## Tax pooling

You can easily save more than 25% of IRD's interest cost on your provisional tax. All with the seal of approval of the IRD.

If you don't pay the correct amount of tax on time the IRD charge you interest. The current rate is 8.89%.

Tax pooling is a service introduced by Inland Revenue that allows provisional taxpayers to reduce their exposure to IRD interest costs.

**How it works:** When we have finished your income tax return, we will inform you whether you owe any further tax to IRD. In many cases, you will also owe IRD interest.

Tax pooling allows you to buy tax credits that other taxpayers do not need. These tax credits have already been paid to IRD, but through the tax pool can be transferred from the seller to you. The cost of buying those credits is substantially less than paying IRD interest. It can also be used to avoid late payment penalties where a payment has been missed.

The table below shows the savings you can make on 2011 underpaid provisional tax if purchased in March 2012.

Underpaid Provisional Tax	Estimated Savings
\$10,000	\$268
\$20,000	\$536
\$30,000	\$803
\$50,000	\$1,338
\$100,000	\$2,675

We can quickly arrange a tax purchase on your behalf as we work closely with NZ's leading tax pooling company, Tax Management NZ. They've assisted thousands of NZ companies and individual provisional taxpayers in saving money. Our fee for this service is \$75 + GST.

## ✓ Financial New Year Checklist!

## Business Perspective

Take the time to consider ways to minimise tax and maximise cash surpluses for the coming year.

### ☐ Will the company make a loss?

File loss offset elections and make subvention payments for the 2011 income year by 31 March 2012.

### ☐ Can you pre-pay expenses?

Many items can be prepaid and claimed as a tax deduction in the year to 31 March 2012.

### ☐ Are you committed to employee expenses?

Amounts owing for holiday pay, bonuses, redundancy payments, long service leave etc. can be claimed, if the employer is committed to them at year end and they're paid within 63 days.

### ☐ Have you scheduled a stock take?

Dispose of obsolete trading stock by 31 March or alternatively write it down to its net realisable value, the lesser of cost or market value.

### ☐ Have you reviewed fixed assets?

If you have assets no longer in use, the book value can be written off - provided the cost of disposal is expected to outweigh the proceeds from its sale, e.g. the keyboard you spilt coffee on.

### ☐ Are repairs and maintenance due?

Consider undertaking repairs and maintenance to key assets before 31 March to ensure a full tax deduction.

### ☐ Do you discount for prompt payment?

You may claim deductions for a discount reserve. In the first year a deduction for the actual discount percentage is allowed. Subsequently the amount is calculated at a percentage level. Different rules apply if credit extended to customers exceeds 93 days.

### ☐ Have you talked to us about the ICA and dividends?

The imputation credit account must balance so there is no debit balance at year end. If you have imputation debit balance, we'll contact you to discuss further.

### ☐ Have you reviewed your debtors' ledger?

To claim a deduction you need to physically write off bad debts in your debtors' ledger before 31 March. You must have taken reasonable steps to recover the debt first.

### ☐ Have you reviewed all contracts?

Have you invoiced retentions that are not due and payable for another year? If they are payable in the current year they need to be declared as income but if not, the income will be deferred to a subsequent year.

### ☐ Have you reviewed all credit notes?

Review credit notes issued to customers after 31 March which might be applied to the previous year, potentially reducing the current year's taxable income.

## Get your docs in a row...

We aim to prepare your financial statements and tax returns in good time. To do this we need your completed annual questionnaires with full supporting documentation. Minimise costly delays by keeping in mind likely supporting documents for:

- ✓ **New Bank Loans**, balance outstanding at year end, security, interest rate, loan term
- ✓ **Fresh Hire Purchases Items**, interest rate, term and repayment plan
- ✓ **Vehicle/Plant & equipment purchases**, agreements. Was finance obtained?
- ✓ **Closing Stock and WIP (Work in Progress)**. Stock on hand at year end? Any un-billed work in progress?
- ✓ **Income**, include details of Wage or Employer Subsidies, additional income as defined for Working for Families

- ✓ **Bank Statements**. If you use MYOB or a similar system, copies of final bank and credit card statements let us check the reconciled balance
- ✓ **Property/Business Sales/Purchases**, agreements and settlement statements
- ✓ **Debtors and Creditors**. What is owed **by** or **to** your business, including whether amounts are GST inclusive or exclusive?
- ✓ **Donations/school fees?** Receipts needed please
- ✓ **Interest, dividends and rebates?** Provide details

### Disclaimer:

*This publication has been carefully prepared, but it has been written in general terms only. The publication should not be relied upon to provide specific information without also obtaining appropriate professional advice after detailed examination of your particular situation.*



## The Vanilla Dream

The vanilla plant flowers just once a year, offering a mere four hours to complete the intricate act of hand pollination. In this window of opportunity a dream has flowered. The Heilala Vanilla story is a PR dream: 100% natural, sustainable, organic, transpacific, sweet and delicious, much like Heilala's own success.

The story begins with John Ross, boat builder, farmer and frequent visitor to Tonga. In 2002, following Cyclone Waka, John recruited six Rotary Club colleagues to deliver medical supplies, help rebuild houses and restore infrastructure to the Tongan village of Utungake in Vava'u. In return, a local chief gifted him the use of dormant land. Upon discovering wild vanilla orchids growing, he developed a vanilla plantation, enhanced job prospects for locals and created Heilala Vanilla.

Producing vanilla seed pods is extremely labour intensive, requiring optimum growing conditions. John engaged the expertise of his son-in-law Garth (agriculturalist and IT consultant) to harness this rare opportunity. They carefully matched organic growing principles with the virgin soil, sustainable coconut husk frames, hand pollination and the Pacific sun, achieving the first Heilala vanilla harvest in 2005 - an admirable 40kg. This grew to two tonne by 2010.

Upon harvest, the vanilla seed pods are imported to Tauranga where the vanilla products are manufactured and packaged per order. They are then dispatched to executive chefs, gourmet food manufacturers and specialty retail outlets.

Heilala Vanilla's growing product range includes vanilla beans, vanilla extract, vanilla paste, vanilla syrup, ground vanilla, vanilla sugar and vanilla ice cream and has received numerous culinary awards.

From the early days of knocking on restaurant doors with a delicious nameless product it was clear they required a strong brand. The challenge would be enlisting the right advocates - the brand needed to entice. Margins are much tighter on small orders, but they knew this temporary pain would spark wildfire momentum and secure the big orders.

### *Heilala {Hey - la - la} - the Tongan national flower*

Down the track, John oversees the Tongan plantation. Garth is in charge of research and product development and daughter Jennifer (a qualified accountant with a marketing degree) is on board to manage sales and marketing. We spoke with Jennifer about their journey to date.

**Biggest challenge?** Giving up the security of her day job. 'But if you have the passion then it's definitely worth it'.

#### **Best management decision?**

Implementing quarterly Client Advisory Boards with specialised 'foodies' to drive their focus and direction. 'In a family business tunnel vision can be a natural stumbling block'.

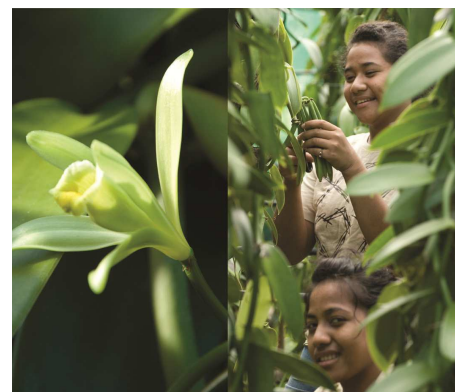
**Advice?** Jennifer was fortunate to utilise her accounting skills within the business, stressing 'every entrepreneur needs guidance, advice and a close relationship with their accountant'. Clearly defined budgets and goals, performance measurement, viability testing and patience are also required for any long term business model.

Jennifer emphasised 'when engaging external services you get what you pay for'. Don't scrimp on the things that support the backbone of your business, whether it be your branding, marketing, or business mentors.

**Highlights so far?** 'Taking Peter Gordon and US pastry chef Natasha MacAller to the Tongan plantation'. The Heilala crew guided 20+ foodies to witness the source of Heilala Vanilla, and enjoy local produce prepared amongst the plantation by Peter and Natasha. Entering the Williams-Sonoma food retail chain (boasting 200 stores across America and Canada) was another memorable milestone.

Having direct ownership of the vanilla seed pods throughout the process, Heilala are proud to have control from plantation to pantry. This ultimately guarantees the quality and integrity of their product.

With each hurdle successfully mounted, the Heilala team keep moving the finish line. As they enter the American market they're aware that initial margins will be tight, sales and profits low. But they'll soon achieve the exposure and reputation their product deserves.



Having John on the ground has been vital to this multi-cultural business. Jennifer and Garth are equally committed to maintaining relationships with the locals, keeping in touch with the dream at its roots. When one day John steps back, their succession plan will have a solid foundation.

The passion, hard work and commitment of this Kiwi family and their Tongan colleagues have made Heilala a sweet story of generosity, imagination and ingenuity. It's about rising to the challenge and seizing the opportunities that are gifted to you.

  
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